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SEC Form 10-K for El Paso Corporation

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Witness _____

Date 7/13/01 Reporter DK

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-K

(Mark One)



**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2000

OR



**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from to

Commission File Number 1-14365

El Paso Corporation

(formerly El Paso Energy Corporation)

(Exact Name of Registrant as Specified in Its Charter)

Delaware

(State or Other Jurisdiction of
Incorporation or Organization)

76-0568816

(I.R.S. Employer
Identification No.)

**El Paso Building
1001 Louisiana Street
Houston, Texas**

(Address of Principal Executive Offices)

77002

(Zip Code)

Registrant's Telephone Number, Including Area Code: (713) 420-2131

Securities registered pursuant to Section 12(b) of the Act:

<u>Title of Each Class</u>	<u>Name of Each Exchange on which Registered</u>
Common Stock, par value \$3 per share	New York Stock Exchange
Preferred Stock Purchase Rights	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
Yes ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

State the aggregate market value of the voting stock held by non-affiliates of the registrant.

Aggregate market value of the voting stock (which consists solely of shares of common stock) held by non-affiliates of the registrant as of March 16, 2001, computed by reference to the closing sale price of the registrant's common stock on the New York Stock Exchange on such date: \$35,108,511,995

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date.

Common Stock, par value \$3 per share. Shares outstanding on March 16, 2001: 508,892,767

Documents Incorporated by Reference

List hereunder the following documents if incorporated by reference and the part of the Form 10-K (e.g., Part I, Part II, etc.) into which the document is incorporated: Portions of our definitive Proxy Statement for the 2001 Annual Meeting of Stockholders, to be filed not later than 120 days after the end of the fiscal year covered by this report, are incorporated by reference into Part III.

EL PASO CORPORATION

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Below is a list of terms that are common to our industry and used throughout this document:

/d	= per day	Mcf	= thousand cubic feet
Bbl	= barrels	Mcfe	= thousand cubic feet of gas equivalents
BBtu	= billion British thermal units	MMcf	= million cubic feet
BBtue	= billion British thermal unit equivalents	MMcfe	= million cubic feet of gas equivalents
Bcf	= billion cubic feet	Mgal	= thousand gallons
MBbls	= thousand barrels	MWh	= megawatt hours
MMBbls	= million barrels	MMWh	= thousand megawatt hours
MMBtu	= million British thermal units	Tcfe	= trillion cubic feet of gas equivalents

When we refer to natural gas and oil in "equivalents," we are doing so to compare quantities of oil with quantities of natural gas or to express these different commodities in a common unit. In calculating equivalents, we use a generally recognized standard in which one Bbl of oil is equal to six Mcf of natural gas. Also, when we refer to cubic feet measurements, all measurements are at 14.73 pounds per square inch.

PART I

ITEM 1. BUSINESS

General

We are a global energy company originally founded in 1928 in El Paso, Texas. For many years, we served as a regional pipeline company conducting business mainly in the western United States. However, over the past five years, we have grown into a company whose operations span the wholesale energy value chain, from natural gas production and extraction to power generation. Our substantial growth during this period has been accomplished through a series of strategic acquisitions, transactions, and internal growth initiatives, each of which has enhanced and improved our competitive abilities in the U.S. and global energy markets. Significant milestones include:

<u>Year</u>	<u>Transaction</u>	<u>Impact</u>
1995	Acquisition of Eastex Energy Inc.	Signaled our entry into the wholesale energy marketing business.
1996	\$4 billion acquisition of the energy businesses of Tenneco Inc.	Expanded our U.S. interstate pipeline system from coast to coast and signaled our entry into the international energy market.
1998	Acquisition of DeepTech International, Inc.	Expanded our U.S. onshore and offshore gathering capacity and capabilities.
1999	\$6 billion merger with Sonat Inc.	Expanded our pipeline operations into the southeast portion of the U.S. and signaled our entrance into the exploration and production business through the addition of 1.5 Tcf of natural gas reserves.
	Creation of \$1.1 billion Electron structure	Provided the vehicle through which we have become a significant non-utility generator of power.
2000	Acquisition of PG&E's Texas Midstream operations	Expanded our midstream operations to cover a majority of the metropolitan markets and industrial hubs in the state of Texas.
2001	Completion of our \$24 billion merger with The Coastal Corporation	This merger places us as a top tier participant in every aspect of the wholesale energy marketplace.

With each significant merger and acquisition, we have evaluated our processes and organizational structure to achieve cost savings and operating efficiencies. These actions have included restructuring our workforce and consolidating our operations. These activities occurred again following the completion of our merger with Coastal in January 2001. Also during this period, we have completed numerous smaller acquisitions and transactions to enhance and expand the scope of our core operations and activities. The discussion of our operations and segments that follows in this document does not include the activities or operations of The Coastal Corporation.

Operations

Our principal operations include:

- the transportation, gathering, processing, and storage of natural gas;
- the marketing of energy and energy-related commodities and products;
- the generation of power;
- the development and operation of energy infrastructure facilities; and
- the exploration and production of natural gas and oil.

Our Pipelines segment owns or has interests in approximately 38,000 miles of interstate natural gas pipelines in the U.S. Our systems connect the nation's principal natural gas supply regions to the five largest consuming regions in the United States: the Gulf Coast, California, the Northeast, the Midwest, and the Southeast. These operations represent one of the largest, and only, integrated coast-to-coast mainline natural gas transmission systems in the U.S. Our pipeline systems also own or have interests in over 150 Bcf of storage capacity used to provide a variety of services to our customers.

Our Merchant Energy segment is involved in a broad range of activities in the energy marketplace including asset ownership, trading and risk management and financial services. We are one of North America's largest wholesale energy commodity marketers and traders, and buy, sell, and trade natural gas, power, and other energy commodities in the U.S. and internationally. We are also a significant non-utility owner of electric generating capacity with 64 facilities in 16 countries. Most recently, we have announced our expansion into the liquefied natural gas business, capitalizing upon the increasing U.S. and worldwide demand for natural gas. The financial services businesses of Merchant Energy invest in emerging businesses to facilitate growth in the U.S. and Canadian energy markets. As a global energy merchant, we evaluate and measure risks inherent in the markets we serve, and use sophisticated systems and integrated risk management techniques to manage those risks.

Our Field Services segment provides natural gas gathering, products extraction, fractionation, dehydration, purification, compression and intrastate transmission services. These services include gathering of natural gas from more than 11,000 natural gas wells with over 19,000 miles of natural gas gathering and natural gas liquids pipelines, and 20 natural gas processing, treating, and fractionation facilities located in some of the most prolific and active production areas in the U.S., including the San Juan Basin, east and south Texas, Louisiana, and the Gulf of Mexico. We conduct our intrastate transmission operations through interests in five intrastate systems, which serve a majority of the metropolitan areas and industrial load centers in Texas. Our primary vehicle for growth and development of midstream energy assets is El Paso Energy Partners, L.P., a publicly traded master limited partnership of which our subsidiary is the general partner. Through Energy Partners, we provide natural gas and oil gathering and transportation, storage, and other related services, principally in the Gulf of Mexico.

Our Production segment leases approximately 2.7 million net acres in 11 states, including Louisiana, New Mexico, Texas, Oklahoma, and Arkansas, as well as the Gulf of Mexico. We also have exploration and production rights in Turkey. During 2000, our daily equivalent natural gas production was approximately 0.6 Bcf/d, and our reserves at December 31, 2000 were approximately 1.7 Tcfe.

In addition to our energy activities, we have announced a telecommunications strategy that will leverage our knowledge of the commodity and capital markets into the emerging telecommunications market. Our strategy involves:

- accessing fiber deep within metropolitan markets to aggregate supply in major U.S. cities;
- utilizing fiber rings and key points of interconnection of major carriers and service providers to allow for liquidity to develop in major markets; and
- assembling a high capacity thin fiber national long-haul backbone.

We will overlay against this asset base a merchant-based operating support system and valuation models that will allow us to apply the merchant skills developed in our core commodity business to the rapidly changing telecommunications markets.

Segments

Our business unit activities are segregated into four primary business segments: Pipelines, Merchant Energy, Field Services, and Production. These segments are strategic business units that provide a variety of energy products and services. During 2000, we combined our International and Merchant Energy segments to reflect the ongoing globalization of our Merchant Energy strategy and its operating activities. We manage each

segment separately and each requires different technology and marketing strategies. Our telecommunication business is combined with our corporate and other activities. For information relating to operating revenues, operating income, EBIT, and identifiable assets by segment, you should see Item 8, Financial Statements and Supplementary Data, Note 15, which is incorporated herein by reference.

Pipelines

Our Pipelines segment provides natural gas transmission services in the U.S. We conduct our activities through five wholly owned and two partially owned interstate systems along with a liquefied natural gas terminalling facility and natural gas storage facilities. Each of these systems is discussed below:

The TGP system. The Tennessee Gas Pipeline system consists of approximately 14,700 miles of pipeline with a design capacity of 5,970 MMcf/d. During 2000, TGP transported natural gas volumes averaging approximately 73 percent of its capacity. This multiple-line system begins in the natural gas-producing regions of Louisiana, including the Gulf of Mexico, and south Texas and extends to the northeast section of the U.S., including the New York City and Boston metropolitan areas. TGP also has an interconnect at the U.S.-Mexico border. Along its system, TGP has approximately 89 Bcf of underground working gas storage capacity.

The EPNG system. The El Paso Natural Gas system consists of approximately 9,800 miles of pipeline with a design capacity of 4,744 MMcf/d. During 2000, EPNG transported natural gas volumes averaging approximately 82 percent of its capacity. The EPNG system delivers natural gas from the San Juan Basin of northern New Mexico and southern Colorado and the Permian Basin and Anadarko Basin to California, which is its single largest market, as well as markets in Nevada, Arizona, New Mexico, Texas, Oklahoma, and northern Mexico.

The SNG system. The Southern Natural Gas system consists of approximately 8,200 miles of pipeline with a design capacity of 2,834 MMcf/d. During 2000, SNG transported volumes averaging approximately 73 percent of its capacity. SNG's interstate pipeline system extends from gas fields in Texas, Louisiana, Mississippi, Alabama and the Gulf of Mexico to markets in Louisiana, Mississippi, Alabama, Florida, Georgia, South Carolina and Tennessee, including the metropolitan areas of Atlanta and Birmingham. SNG is the principal pipeline supplier to the growing southeastern markets of Alabama and Georgia. In August 2000, the South Georgia Natural Gas system was combined with the SNG system as part of SNG's rate case settlement. Along its system, SNG has approximately 60 Bcf of underground working gas storage capacity.

The Midwestern system. The Midwestern system consists of approximately 400 miles of pipeline with a design capacity of 785 MMcf/d. During 2000, Midwestern transported natural gas volumes averaging approximately 33 percent of its capacity. The Midwestern system connects with the TGP system at Portland, Tennessee, and extends to Chicago to serve the Chicago metropolitan area. As a result of our merger with Coastal in January 2001, we will be required to sell the Midwestern system. We expect to complete the sale in the second quarter of 2001.

The MPC system. The Mojave Pipeline Company system consists of approximately 400 miles of pipeline with a design capacity of approximately 400 MMcf/d. During 2000, MPC transported natural gas volumes approximating 100 percent of its capacity. The MPC system connects with the EPNG transmission system at Topock, Arizona and the Kern River Gas Transmission Company system in California and extends to customers in the vicinity of Bakersfield, California.

Florida Gas Transmission system. We own a 50 percent interest in Citrus Corp., a holding company that owns 100 percent of Florida Gas Transmission Company. Florida Gas is the primary pipeline transporter of natural gas in the state of Florida and the sole pipeline transporter to peninsular Florida. The system consists of approximately 4,800 miles of interstate natural gas pipelines with a design capacity of 1,462 MMcf/d. During 2000, Florida Gas transported volumes averaging approximately 92 percent of its capacity. The system extends from south Texas to a point near Miami, Florida.

Portland Natural Gas Transmission. We own an approximate 19 percent interest in the Portland Natural Gas Transmission system. Portland consists of approximately 300 miles of interstate natural gas pipeline with a design capacity of 215 MMcf/d extending from the Canadian border near Pittsburg, New Hampshire to Dracut, Massachusetts. During 2000, Portland transported volumes averaging approximately 51 percent of its capacity.

Southern LNG, Inc. Southern LNG owns a liquefied natural gas receiving terminal, located on Elba Island, near Savannah, Georgia, capable of achieving a peak send out of 540 MMcf/d and a base load send out of 333 MMcf/d. Inactive since the early 1980s, Southern LNG received an order from the Federal Energy Regulatory Commission (FERC) in March 2000 granting it permission to reactivate the receiving terminal. We expect the terminal to be in service in the fourth quarter of 2001.

Bear Creek Storage. Bear Creek Storage Company owns and operates an underground natural gas storage facility located in Louisiana. The facility has a capacity of 50 Bcf of base gas and 58 Bcf of working storage. Bear Creek's working storage capacity is committed equally to the TGP and SNG systems under long-term contracts.

Regulatory Environment

Our interstate natural gas systems and storage operations are regulated by FERC under the Natural Gas Act of 1938 and the Natural Gas Policy Act of 1978. Each system operates under separate FERC approved tariffs that establish rates, terms, and conditions under which each system provides services to its customers. Generally, FERC's authority extends to:

- transportation of natural gas, rates, and charges;
- certification and construction of new facilities;
- extension or abandonment of services and facilities;
- maintenance of accounts and records;
- depreciation and amortization policies;
- acquisition and disposition of facilities;
- initiation and discontinuation of services; and
- various other matters.

Our wholly owned and investee pipelines have tariffs established through filings with FERC that have a variety of terms and conditions, each of which affects its operations and its ability to recover fees for the services it provides. By and large, changes to these fees or terms can only be implemented upon approval by FERC.

Our interstate pipeline systems are also subject to the Natural Gas Pipeline Safety Act of 1968 that establishes pipeline and liquefied natural gas plant safety requirements, the National Environmental Policy Act, and other environmental legislation. Each of our systems has a continuing program of inspection designed to keep all of our facilities in compliance with pollution control and pipeline safety requirements. We believe that our systems are in substantial compliance with the applicable requirements.

For a further discussion of significant rate and regulatory matters, see Item 8, Financial Statements and Supplementary Data, Note 11.

Markets and Competition

Our interstate systems face varying degrees of competition from alternative energy sources, such as electricity, hydroelectric power, coal, and fuel oil. Also, the potential consequences of proposed and ongoing restructuring and deregulation of the electric power industry are currently unclear. Restructuring and deregulation may benefit the natural gas industry by creating more demand for natural gas turbine generated

electric power, or it may hamper demand by allowing a more effective use of surplus electric capacity through increased wheeling as a result of open access.

TGP. TGP's customers include natural gas producers, marketers and end-users, as well as other gas transmission and distribution companies, none of which individually represents more than 10 percent of the revenues on TGP's system. Currently, over 70 percent of TGP's capacity is subject to firm contracts expiring after 2001. These contracts have an average term in excess of five years. TGP continues to pursue future markets and customers for the capacity that is not committed beyond 2001 and expects this capacity will be placed under a combination of long-term and short-term contracts. However, there can be no assurance that TGP will be able to replace these contracts or that the terms of new contracts will be as favorable to TGP as the existing ones.

In a number of key markets, TGP faces competitive pressures from other major pipeline systems, which enable local distribution companies and end-users to choose a supplier or switch suppliers based on the short-term price of natural gas and the cost of transportation. Competition among pipelines is particularly intense in TGP's supply areas, Louisiana and Texas. In some instances, TGP has had to discount its transportation rates in order to maintain market share. The renegotiation of TGP's expiring contracts may be adversely affected by these competitive factors.

EPNG. EPNG faces competition from other pipeline companies that transport natural gas to the California market. EPNG's current capacity to deliver natural gas to California is approximately 3.3 Bcf/d, and the combined capacity of all pipeline companies serving the California market is approximately 6.9 Bcf/d. In 2000, the demand for interstate pipeline capacity to California averaged 5.4 Bcf/d, equivalent to approximately 78 percent of the total interstate pipeline capacity serving that state. Natural gas shipped to California across the EPNG system represented approximately 35 percent of the natural gas consumed in the state in 2000. EPNG's ability to remarket its capacity under expiring contracts may be adversely affected by excess capacity into California.

The significant customers served by EPNG in California during 2000 included Southern California Gas Company, with capacity of 1,150 MMcf/d under contract until August 2006, and Merchant Energy, with capacity of 1,221 MMcf/d under contract through May 2001. In February 2001, EPNG completed its open season on the capacity held by Merchant Energy and all of the available capacity was re-subscribed. Contracts were awarded to 30 different entities, including 271 MMcf/d to Merchant Energy, all at published tariff rates under contracts with durations from 17 months to 15 years.

SNG. SNG's customers include distribution and industrial customers, electric generation companies, gas producers, other gas pipelines and gas marketing and trading companies. SNG provides transportation services in both its natural gas supply and market areas. SNG's contracts to provide firm transportation service for its customers are for varying amounts and periods of time. Substantially all of the firm transportation capacity currently available in SNG's two largest market areas is fully subscribed. The significant customers served by SNG include:

- Atlanta Gas Light Company, with capacity of 770 MMcf/d under contracts that expire beginning in 2005 through 2007, with the majority expiring in 2005;
- Alabama Gas Corporation, with capacity of 384 MMcf/d under contracts that expire beginning in 2005 through 2008, with the majority expiring in 2008; and
- South Carolina Pipeline Corporation, with capacity of 188 MMcf/d under contract which expires primarily in 2005.

Nearly all of SNG's firm transportation contracts automatically extend the term for additional months or years unless notice of termination is given by one of the parties.

Competition among pipelines is strong in a number of SNG's key markets. Customers purchase natural gas supply from producers and natural gas marketing companies in unregulated transactions and contract with SNG for transportation services to deliver this supply to their markets. SNG's three largest customers are able

to obtain a significant portion of their natural gas requirements through transportation from other pipelines. In addition, SNG competes with several pipelines for the transportation business of many of its other customers. The competition with such pipelines is intense, and SNG must, at times, discount its transportation rates in order to maintain market share.

Merchant Energy

Our Merchant Energy segment is a market maker involved in a broad range of activities in the wholesale energy marketplace, including asset ownership, trading and risk management, and financial services. Merchant Energy is organized into six functional units, each with complementary activities that support our overall global merchant energy model. These units are:

- Marketing and Origination;
- Trading and Risk Management;
- Power Generation;
- LNG;
- Financial Services; and
- Operations.

Marketing and Origination. The Marketing and Origination unit provides energy solutions in natural gas, power, and other energy commodity markets. This unit also markets capacity from power and natural gas assets, and creates innovative structured transactions to enhance the value of Merchant Energy's assets. This unit is able to provide its customers with flexible solutions to meet their energy supply and financial risk management requirements by utilizing its knowledge of the marketplace, natural gas pipelines, storage, and power transmission infrastructures, supply aggregation, transportation management and valuation, and integrated price risk management. They also enter into short and long term energy supply and purchase contracts and perform total energy infrastructure outsourcing for customers.

Trading and Risk Management. The Trading and Risk Management unit trades natural gas, power, other energy commodities, and related financial instruments in North America and Europe and provides pricing and valuation analysis for the Marketing and Origination unit. Using the financial markets, this unit manages the inherent risk of Merchant Energy's asset and trading portfolios using value-at-risk limits set by our Board of Directors and optimizes the value inherent in the segment's asset portfolio.

During 2000, the Marketing and Origination and Trading and Risk Management units grew their combined physical and financially settled volumes by approximately 40% to 106,656 BBtue/d. Power marketed during 2000 increased by over 43 percent. We expect our marketed volumes to significantly increase in 2001.

Marketing and trading energy commodity volumes for the years ended December 31 were:

	2000	1999	1998
Physical natural gas marketed (Bbtu/d)	6,899	6,713	7,089
Power marketed (MMWh)	113,652	79,361	55,210
Financial settled volumes (BBtue/d)	98,574	68,678	31,793

Power Generation. Our Power Generation unit is one of the largest non-utility generators in the U.S., and currently owns or has interests in 64 power plants in 16 countries. These plants represent 17,153 gross megawatts of generating capacity. Of these facilities, 75 percent are natural gas fired, 15 percent are geothermal, with the remaining 10 percent utilizing natural gas liquids, coal, and other fuels. During 2000, Merchant Energy continued acquiring domestic non-utility generation (NUG) assets, especially those with above-market power purchase agreements. As part of these efforts, we used Chaparral Investors, L.L.C. (also referred to as Electron) to expand Merchant Energy's growth in the power generation business. Through Chaparral, Merchant Energy has invested in 27 U.S. power generation facilities with a total generating capacity of approximately 5,600 gross megawatts. A subsidiary of Merchant Energy serves as the manager of Chaparral and its wholly-owned subsidiary, Mesquite Investors, L.L.C., under a management agreement, which expires in 2006. As compensation for managing Chaparral, Merchant Energy is paid an annual performance-based management fee.

Detailed below are brief descriptions, by region, of Merchant Energy's power generation projects that are either operational or in various stages of construction or development.

<u>Region</u>	<u>Project Status</u>	<u>Number of Facilities</u>	<u>Gross Megawatts</u>
North America			
East Coast	Operational	13	3,263
	Under Construction	1	716
	Under Development	3	1,664
Central	Operational	7	1,253
West Coast	Operational	21	1,036
South America	Operational	7	4,114
	Under Construction	1	470
Asia	Operational	5	2,589
	Under Construction	2	1,108
Europe	Operational	3	544
	Under Construction	1	396
Total		<u>64</u>	<u>17,153</u>

LNG. The LNG unit contracts for LNG terminalling and regasification capacity, coordinates short and long term LNG supply deliveries, and is developing an international LNG supply and marketing business. As of December 31, 2000, our LNG unit has contracted for over 280 Bcf per year of LNG regasification capacity at three locations along the Eastern Coast of the U.S. and one location in Louisiana. In the Caribbean, we have contracted for 105 Bcf per year of long term supplies of LNG with deliveries scheduled to begin in 2002.

Financial Services. The Financial Services unit provides financing to the energy and power industries and provides institutional funds management. Merchant Energy owns EnCap, an institutional funds management firm specializing in financing independent oil and natural gas producers. EnCap manages three separate institutional oil and natural gas investment funds in the U.S., and serves as investment advisor to Energy Capital Investment Company PLC, a publicly traded investment company in the United Kingdom. During 2000, we acquired Enerplus Global Energy Management, Inc., an institutional and retail funds management firm in Canada. Combined, EnCap and Enerplus manage funds with a market value of approximately \$2 billion. In addition to EnCap and Enerplus, Merchant Energy's Financial Services unit holds investments of approximately \$62 million. Also in 2000, it began originating financing for North American power development projects. As of December 31, 2000, it had funded \$5 million of loans with additional commitments for \$68 million.

Operations. The Operations unit conducts the day-to-day operations of Merchant Energy's assets in close coordination with the Marketing and Origination, and Trading and Risk Management units. Our Operations unit operates 13 generating facilities in the U.S. and three facilities in two foreign countries.

Finance and Administration. In addition to its functional units, Merchant Energy has a Finance and Administration unit that implements financing strategies for its assets, and provides accounting and administrative services for the segment's activities.

Regulatory Environment

Merchant Energy's domestic power generation activities are regulated by FERC under the Federal Power Act with respect to its rates, terms, and conditions of service and other reporting requirements. In addition, exports of electricity outside of the U.S. must be approved by the Department of Energy. Its cogeneration power production activities are regulated by FERC under the Public Utility Regulatory Policies Act with respect to rates, procurement and provision of services, and operating standards. All of its power generation activities are also subject to U.S. Environmental Protection Agency (EPA) regulations.

Merchant Energy's foreign operations are regulated by numerous governmental agencies in the countries in which these projects are located. Generally, many of the countries in which Merchant Energy conducts and will conduct business have recently developed or are developing new regulatory and legal structures to accommodate private and foreign-owned businesses. These regulatory and legal structures and their interpretation and application by administrative agencies are relatively new and sometimes limited. Many detailed rules and procedures are yet to be issued and we expect that the interpretation of existing rules in these jurisdictions will evolve over time. We believe that our operations are in compliance in all material respects with all applicable environmental laws and regulations in the applicable foreign jurisdictions. We also believe that the operations of our projects in many of these countries eventually may be required to meet standards that are comparable in many respects to those in effect in the U.S. and in countries within the European Community.

Markets and Competition

Merchant Energy maintains a diverse supplier and customer base. During 2000, Merchant Energy's activities served over 900 suppliers and over 1,300 sales customers around the world.

Merchant Energy's trading, marketing, and power development businesses operate in a highly competitive environment. Its primary competitors include:

- affiliates of major oil and natural gas producers;
- multi-national energy infrastructure companies;
- large domestic and foreign utility companies;
- affiliates of large local distribution companies;
- affiliates of other interstate and intrastate pipelines; and
- independent energy marketers and power producers with varying scopes of operations and financial resources.

Merchant Energy competes on the basis of price, access to production, understanding of pipeline and transmission networks, imbalance management, experience in the marketplace, and counterparty credit.

Many of Merchant Energy's generation facilities sell power pursuant to long-term agreements with investor-owned utilities in the U.S. Because of the terms of its power purchase agreements for its facilities, Merchant Energy's revenues are not significantly impacted by competition from other sources of generation for these facilities. The power generation industry is rapidly evolving, and regulatory initiatives have been adopted at the federal and state level aimed at increasing competition in the power generation business. As a result, it is likely that when the power purchase agreements expire, these facilities will be required to compete in a significantly different market in which operating efficiency and other economic factors will determine success. Merchant Energy is likely to face intense competition from generation companies as well as from the wholesale power markets. The successful acquisition of new business opportunities is dependent upon Merchant Energy's ability to respond to requests to provide new services, mitigate potential risks, and maintain strong business development, legal, financial, and operational support teams with experience in the respective marketplace.

Field Services

Our Field Services segment provides customers with wellhead-to-mainline services, including natural gas gathering, storage, products extraction, fractionation, dehydration, purification, compression, transportation of natural gas and natural gas liquids, and intrastate natural gas transmission services. It also provides well-ties and offers real-time information services, including electronic wellhead gas flow measurement, and works with Merchant Energy to provide fully bundled natural gas services with a broad range of pricing options as well as financial risk management products.

Field Services' assets include natural gas gathering and natural gas liquids pipelines, treating, processing, and fractionation facilities in the San Juan Basin, the producing regions of east and south Texas, and Louisiana.

Through our subsidiaries, we own a one percent general partner interest in Energy Partners and a one percent non-managing interest in many of its subsidiaries. We also own 27.8 percent of the partnership's common units and \$170 million of its preferred units. Energy Partners is our primary vehicle for the acquisition and development of midstream energy infrastructure assets. Energy Partners' assets provide gathering, transportation, storage, and other related activities for producers of natural gas and oil. Energy Partners owns or has interests in twelve natural gas and oil pipeline systems, seven offshore platforms, two natural gas storage facilities, five producing oil and natural gas properties, and an overriding royalty interest in a non-producing oil and natural gas property. As a result of our merger with Coastal in January 2001, Energy Partners sold its interests in several assets in the Gulf of Mexico. These sales consisted of interests in seven natural gas pipeline systems, a dehydration facility and two offshore platforms. Energy Partners completed these sales in March of 2001.

In December 2000, Field Services purchased PG&E's Texas Midstream operations. The acquired assets consisted of 7,500 miles of natural gas transmission and natural gas liquids pipelines that transport approximately 2.8 Bcf/d, nine natural gas processing and fractionation plants that process 1.5 Bcf/d, and rights to 7.2 Bcf of natural gas storage capacity. These assets serve a majority of the metropolitan areas and the largest industrial load centers in Texas, as well as numerous natural gas trading hubs. These assets also create a physical link between our EPNG and TGP systems. In the first quarter of 2001, Field Services sold some of these acquired natural gas liquids transportation and fractionation assets to Energy Partners. The assets sold included more than 600 miles of natural gas liquids gathering and transportation pipelines and three fractionation plants located in south Texas.

The following tables provide information concerning Field Services' natural gas gathering and transportation facilities, its processing facilities, and its facilities accounted for under the equity method as of and for each of the three years ended December 31:

Gathering & Treating	Miles of Pipeline ⁽¹⁾	Throughput Capacity (MMcfe/d) ⁽²⁾	Average Throughput (BBtue/d) ⁽³⁾			Percent of Ownership Interest
			2000	1999	1998	
Western Division	5,555	1,200	1,237	1,262	1,191	100
Eastern Division	1,251	909	271	386	424	100
Central Division ⁽³⁾	9,890	6,760	1,425	1,528	1,771	100
Energy Partners ⁽⁴⁾⁽⁵⁾	2,076	1,545	774	698	695	30
Oasis ⁽⁶⁾	608	350	268	263	289	—
Viosca Knoll ⁽⁵⁾	125	10	6	142	287	—

Processing Plants	Inlet Capacity ⁽²⁾ (MMcf/d)	Avg. Inlet Volume (BBtu/d) ⁽²⁾			Average Natural Gas Liquids Sales (Mgal/d)			Percent of Ownership Interest
		2000	1999	1998	2000	1999	1998	
Western Division	600	635	650	586	384	432	370	100
Eastern Division	369	121	140	160	222	264	349	100
Central Division ⁽³⁾	1,883	309	242	269	307	202	208	100
Coyote Gulch	120	87	97	69	—	—	—	50

⁽¹⁾ Mileage amounts are approximate for the total systems and have not been reduced to reflect Field Services' net ownership.

⁽²⁾ All volumetric information reflects Field Services' net interest and is subject to increases or decreases depending on operating pressures and point of delivery into or out of the system.

⁽³⁾ Reflects the acquisition of PG&E's Texas Midstream operations in December 2000.

⁽⁴⁾ In the first quarter of 2001, Energy Partners sold their interests in several of its gathering, transmission, and treating systems in the Gulf of Mexico. Total miles of the pipelines sold were 881. Our net interest in these systems included combined throughput capacity of 542 MMcfe/d and average throughput for the years ended December 31, 2000, 1999, and 1998 of 241 BBtue/d, 277 BBtue/d, and 330 BBtue/d.

⁽⁵⁾ Field Services sold its 49 percent interest in Viosca Knoll to Energy Partners in June 1999 and its remaining one percent interest in September 2000.

⁽⁶⁾ Field Services sold its 35 percent interest in Oasis in December 2000.

Regulatory Environment

Some of Field Services' and Energy Partners' operations are subject to regulation by FERC in accordance with the Natural Gas Act of 1938 and the Natural Gas Policy Act of 1978. Each pipeline subject to regulation operates under separate FERC approved tariffs with established rates, terms and conditions under which the pipeline provides services.

In addition, some of Field Services' and Energy Partners' operations, directly owned or owned through equity investments, are subject to the Natural Gas Pipeline Safety Act of 1968, the Hazardous Liquid Pipeline Safety Act, and the National Environmental Policy Act. Each of the pipelines has a continuing program of inspection designed to keep all of the facilities in compliance with pollution control and pipeline safety requirements and Field Services and Energy Partners believe that these systems are in substantial compliance with applicable requirements.

Markets and Competition

Field Services competes with, among others, major interstate and intrastate pipeline companies in the transportation of natural gas and natural gas liquids. Field Services also competes with major integrated energy companies, independent natural gas gathering and processing companies, natural gas marketers, and oil and natural gas producers in gathering and processing natural gas and natural gas liquids. Competition for throughput and natural gas supplies is based on a number of factors, including price, efficiency of facilities,

gathering system line pressures, availability of facilities near drilling activity, service, and access to favorable downstream markets.

Production

Our Production segment is engaged in the exploration for and the acquisition, development, and production of natural gas, oil, and natural gas liquids in the major producing basins of the United States. Production has onshore and coal seam operations and properties in 11 states and offshore operations and properties in federal and state waters in the Gulf of Mexico. It also has exploration and production rights in Turkey.

Production sells its natural gas primarily at spot-market prices. It sells its natural gas liquids at market prices under monthly or long-term contracts and its oil production at posted prices, subject to adjustments for gravity and transportation. Production engages in hedging activities on its natural gas and oil production in order to stabilize cash flows and reduce the risk of downward commodity price movements on sales of its production. A significant portion of the segment's 2000 production was hedged by entering into third-party contracts and forward sales.

Strategically, Production emphasizes disciplined investment criteria and manages its existing production portfolio to maximize volumes and minimize costs. Production expects to continue an active onshore and offshore drilling program to capitalize on its land and seismic holdings. Production is also pursuing strategic acquisitions of producing properties and the development of coal seam projects. In 2000, Production replaced 229 percent of the reserves it produced.

Natural Gas and Oil Reserves

The following table details Production's proved reserves at December 31, 2000. Information in the table is based upon the reserve report prepared by Production dated January 1, 2001, and agrees with Production's estimate of reserves filed with other federal agencies except for differences of less than 5 percent resulting from actual production, acquisitions, property sales, and necessary reserve revisions and additions to reflect actual experience.

	Net Proved Reserves ⁽¹⁾		
	Natural Gas (MMcf)	Liquids ⁽²⁾ (MBbls)	Total (MMcfe)
Producing	912,567	13,672	994,598
Non-Producing	148,887	4,969	178,698
Undeveloped	490,882	11,854	562,008
Total proved reserves	1,552,336	30,495	1,735,304

⁽¹⁾ Net proved reserves exclude royalties and interests owned by others and reflects contractual arrangements and royalty obligations in effect at the time of the estimate.

⁽²⁾ Includes oil, condensate, and natural gas liquids.

There are numerous uncertainties inherent in estimating quantities of proved reserves and in projecting future rates of production and timing of development expenditures, including many factors beyond the control of Production. The reserve data represents only estimates. Reservoir engineering is a subjective process of estimating underground accumulations of natural gas and oil that cannot be measured in an exact manner. The accuracy of any reserve estimate is a function of the quality of available data and of engineering and geological interpretations and judgment. As a result, estimates of different engineers often vary. In addition, results of drilling, testing, and production subsequent to the date of an estimate may justify revision of such estimate. Reserve estimates are often different from the quantities of natural gas and oil that are ultimately recovered. The meaningfulness of reserve estimates is highly dependent upon the accuracy of the assumptions upon which they were based. In general, the volume of production from natural gas and oil properties owned

by Production declines as reserves are depleted. Except to the extent Production conducts successful exploration and development activities or acquires additional properties containing proved reserves, or both, the proved reserves of Production will decline as reserves are produced.

For further discussion of our reserves, see Item 8, Financial Statements and Supplementary Data, Note 19.

Wells and Acreage

The following table details Production's gross and net interest in developed and undeveloped onshore, offshore, and coal seam acreage at December 31, 2000. Any acreage in which Production's interest is limited to owned royalty, overriding royalty, and other similar interests is excluded.

	Developed		Undeveloped		Total	
	Gross	Net	Gross	Net	Gross	Net
Onshore	488,988	297,334	946,288	668,537	1,435,276	965,871
Offshore	292,660	196,525	1,087,567	1,040,145	1,380,227	1,236,670
Coal seam	32,634	26,666	581,045	437,493	613,679	464,159
Total	<u>814,282</u>	<u>520,525</u>	<u>2,614,900</u>	<u>2,146,175</u>	<u>3,429,182</u>	<u>2,666,700</u>

The domestic net developed acreage is concentrated primarily in the Gulf of Mexico (38 percent), Texas (21 percent), Oklahoma (18 percent), and Louisiana (18 percent). Approximately 19 percent, 18 percent, and 5 percent of our total domestic net undeveloped acreage is under leases that have minimum remaining primary terms expiring in 2001, 2002, and 2003.

The following table details Production's working interests in onshore, offshore, and coal seam natural gas and oil wells at December 31, 2000. Gross wells include 21 multiple completions.

	Productive Natural Gas Wells		Productive Oil Wells		Total Productive Wells		Number of Wells Being Drilled	
	Gross	Net	Gross	Net	Gross	Net	Gross	Net
Onshore	1,393	967	27	25	1,420	992	20	12
Offshore	144	60	15	12	159	72	1	1
Coal seam	<u>1,042</u>	<u>652</u>	<u>—</u>	<u>—</u>	<u>1,042</u>	<u>652</u>	<u>57</u>	<u>41</u>
Total	<u>2,579</u>	<u>1,679</u>	<u>42</u>	<u>37</u>	<u>2,621</u>	<u>1,716</u>	<u>78</u>	<u>54</u>

The following table details Production's exploratory and development wells drilled during the years 1998 through 2000.

	Net Exploratory Wells Drilled			Net Development Wells Drilled		
	2000	1999	1998	2000	1999	1998
Productive	5	12	15	199	116	204
Dry	<u>11</u>	<u>14</u>	<u>19</u>	<u>5</u>	<u>2</u>	<u>18</u>
Total	<u>16</u>	<u>26</u>	<u>34</u>	<u>204</u>	<u>118</u>	<u>222</u>

The information above should not be considered indicative of future drilling performance, nor should it be assumed that there is any correlation between the number of productive wells drilled and the amount of natural gas and oil that may ultimately be recovered.

Net Production, Unit Prices, and Production Costs

The following table details Production's net production volumes, average sales prices received, and average production costs associated with the sale of natural gas and oil for each of the years ended December 31:

	<u>2000</u>	<u>1999</u>	<u>1998</u>
Net Production:			
Natural Gas (Bcf)	188	186	226
Oil, Condensate, and Liquids (MMBbls)	5	6	8
Total (Bcfe)	219	221	276
Average Realized Sales Price:			
Natural Gas (\$/Mcf)	\$ 2.26	\$ 2.05	\$ 1.95
Oil, Condensate, and Liquids (\$/Bbl)	\$17.98	\$15.46	\$12.22
Average Production Cost (\$/Mcfe) ⁽¹⁾	\$ 0.34	\$ 0.44	\$ 0.33

⁽¹⁾ Includes direct lifting costs (labor, repairs and maintenance, materials, and supplies) and the administrative costs of production offices, insurance, and property and severance taxes.

Acquisition, Development, and Exploration Expenditures

The following table details information regarding Production's costs incurred in its development, exploration, and acquisition activities during each of the years ended December 31:

	<u>2000</u>	<u>1999</u>	<u>1998</u>
	<u>(In millions)</u>		
Acquisition Costs:			
Proved	\$ 74	\$ 3	\$ 2
Unproved	41	45	48
Development Costs	269	178	375
Exploration Costs:			
Delay Rentals	6	7	11
Seismic Acquisition and Reprocessing	13	58	53
Drilling	81	74	92
Total Capital Expenditures	<u>\$484</u>	<u>\$365</u>	<u>\$581</u>

Regulatory and Operating Environment

The federal government and the states in which Production operates or owns interests in producing properties regulate various matters affecting natural gas and oil production, including drilling and spacing of wells, conservation, forced pooling, and protection of correlative rights among interest owners. Production is also subject to governmental safety regulations in the jurisdictions in which it operates.

Production's operations under federal natural gas and oil leases are regulated by the statutes and regulations of the United States Department of the Interior that currently impose liability upon lessees for the cost of pollution resulting from their operations. Royalty obligations on all federal leases are regulated by the Minerals Management Service, which has promulgated valuation guidelines for the payment of royalties by producers. Other federal, state, and local laws and regulations relating to the protection of the environment affect Production's natural gas and oil operations through their effect on the construction and operation of facilities, drilling operations, production, or the delay or prevention of future offshore lease sales. We maintain substantial insurance on behalf of Production for sudden and accidental spills and oil pollution liability.

Production's business has operating risks normally associated with the exploration for and production of natural gas and oil, including blowouts, cratering, pollution, and fires, each of which could result in damage to life or property. Offshore operations may encounter usual marine perils, including hurricanes and other adverse weather conditions, and governmental regulations as well as interruption or termination by

governmental authorities based on environmental and other considerations. Customary with industry practices, we maintain broad insurance coverage on behalf of Production with respect to potential losses resulting from these operating hazards.

Markets and Competition

The natural gas and oil business is highly competitive in the search for and acquisition of additional reserves and in the sale of natural gas, oil, and liquids. Production's competitors include major and intermediate sized oil and natural gas companies, independent oil and natural gas operations, and individual producers or operators with varying scopes of operations and financial resources. Competitive factors include price, contract terms, and quality of service. To some degree, price competition is mitigated by Production's hedging activities.

Corporate and Other Operations

Through our corporate group, we perform management, legal, financial, tax, consulting, administrative and other services for our operating business segments. The costs of providing these services are allocated to our business segments. Our other operations include the assets and operations of our telecommunications business.

Environmental

A description of our environmental activities is included in Item 8, Financial Statements and Supplementary Data, Note 11, and is incorporated by reference herein.

Employees

As of March 19, 2001, including the employees we acquired as a result of our merger with Coastal, we had approximately 15,000 full-time employees, of which 600 are subject to collective bargaining arrangements.

Executive Officers of the Registrant

Our executive officers as of March 19, 2001, are listed below. Prior to August 1, 1998, all references to El Paso refer to positions held with El Paso Natural Gas Company.

<u>Name</u>	<u>Office</u>	<u>Officer Since</u>	<u>Age</u>
William A. Wise	Chairman, President, and Chief Executive Officer of El Paso	1983	55
H. Brent Austin	Executive Vice President and Chief Financial Officer of El Paso	1992	46
Ralph Eads	Executive Vice President of El Paso and President of El Paso's Merchant Energy Group	1999	41
Joel Richards III	Executive Vice President of El Paso	1990	54
John W. Somerhalder II	Executive Vice President of El Paso and President of El Paso's Pipeline Group	1990	45
Britton White Jr.	Executive Vice President and General Counsel of El Paso	1991	57
Rodney D. Erskine	President of El Paso Production	2001	56
John D. Hushon	President of El Paso Merchant Energy Europe	1996	55
Greg G. Jenkins	President of El Paso Global Networks	1996	43
Byron R. Kelley	President of El Paso Energy International	2001	53
Robert G. Phillips	President of El Paso Field Services	1995	46
Clark C. Smith	President of El Paso Merchant Energy North America	2000	46
William A. Smith	President of El Paso Global LNG	1999	56
Tom M. Wade	President of Petroleum Markets	2001	48

Mr. Wise has been Chief Executive Officer since January 1990 and the Chairman of the Board of Directors since January 2001. He was also Chairman of the Board from January 1994 until October 1999. Mr. Wise became the President of El Paso in July 1998 and also served in that capacity from January 1990 to April 1996. Mr. Wise is a member of the Board of Directors of Battle Mountain Gold Company and is the Chairman of the Board of El Paso Tennessee Pipeline Co. and El Paso Energy Partners Company, the general partner of Energy Partners.

Mr. Austin has been an Executive Vice President since May 1995. He has been our Chief Financial Officer since April 1992. Prior to that period, he served in various positions with Burlington Resources Inc.

Mr. Eads has been an Executive Vice President since July 1999 and President of the El Paso Merchant Energy Group since January 2001. Mr. Eads was a Managing Director and Co-Head of the Energy Group at Donaldson, Lufkin & Jenrette from January 1996 through June 1999. Prior to that period, he was Managing Director, Head of Energy at S.G. Warburg Company.

Mr. Richards has been an Executive Vice President since December 1996. From January 1991 until December 1996, he was a Senior Vice President of El Paso.

Mr. Somerhalder has been an Executive Vice President of El Paso since April 2000, and President of our Pipeline segment since January 2001. He has been Chairman of the Board of TGP, EPNG, and SNG since January 2000. He was President of TGP from December 1996 to January 2000, President of El Paso Energy Resources Company from April 1996 to December 1996 and a Senior Vice President of El Paso from August 1992 to April 1996.

Mr. White has been an Executive Vice President of El Paso and General Counsel since December 1996. Prior to that period, he was a Senior Vice President and General Counsel of El Paso.

Mr. Erskine has been President of El Paso Production since our merger with Coastal in January 2001. He was Senior Vice President of Coastal from August 1997. He has held various positions with Coastal Oil & Gas Corporation, a subsidiary of Coastal, since 1994.

Mr. Hushon has been President of El Paso Merchant Energy Europe since January 2001. He was President of El Paso International from April 1996 to January 2001. He was Senior Vice President of El Paso International from September 1995 to April 1996. Prior to that period, Mr. Hushon was a senior partner in the law firm of Arent Fox Kintner Plotkin & Kahn.

Mr. Jenkins has been President of El Paso Global Networks since August 2000. He was President of Merchant Energy from December 1996 to August 2000. He was Senior Vice President and General Manager of Entergy Corp. from May 1996 to December 1996. Prior to that period, he was President and Chief Executive Officer of Hadson Gas Services Company.

Mr. Kelley has been President of El Paso International since January 2001. He was Executive Vice President of Business Development and commercial management for El Paso International since 1996. Prior to that period, Mr. Kelley held various positions with Tenneco Energy.

Mr. Phillips has been President of El Paso Field Services since June 1997. He was President of El Paso Energy Resources Company from December 1996 to June 1997, President of Field Services from April 1996 to December 1996 and was a Senior Vice President of El Paso from September 1995 to April 1996. Prior to that period, Mr. Phillips was Chief Executive Officer of Eastex Energy, Inc.

Mr. Clark C. Smith has been President of El Paso Merchant Energy North America since August 2000. He served as President and CEO of Engage Energy Inc. since 1997. Prior to that period, he held the position of President and CEO of Coastal Gas Marketing Company and held several positions with Enron Corp.

Mr. William A. Smith has been President of El Paso Global LNG since March 2001. He was an Executive Vice President of El Paso from October 1999 to March 2001. He was Executive Vice President and General Counsel of Sonat Inc. from 1995 to September 1999. He was Vice Chairman of Sonat Exploration from 1994 to 1995 and Chairman and President of SNG from 1989 to 1994.

Mr. Wade has been President of Petroleum Markets since January 2001. He has held various positions with Coastal since 1980.

Executive officers hold offices until their successors are elected and qualified, subject to their earlier removal.

ITEM 2. PROPERTIES

A description of our properties is included in Item 1, Business, and is incorporated by reference herein.

We are of the opinion that we have satisfactory title to the properties owned and used in our businesses, subject to liens for current taxes, liens incident to minor encumbrances, and easements and restrictions that do not materially detract from the value of such property or the interests therein or the use of such properties in our businesses. We believe that our physical properties are adequate and suitable for the conduct of our business in the future.

ITEM 3. LEGAL PROCEEDINGS

See Item 8, Financial Statements and Supplementary Data, Note 11, which is incorporated herein by reference.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Our common stock is traded on the New York Stock Exchange under the symbol EPG. As of March 16, 2001, we had 68,070 stockholders of record. This does not include individual participants who own our common stock, but whose shares are held by a clearing agency, such as a broker or bank.

The following table reflects the quarterly high and low sales prices for our common stock based on the daily composite listing of stock transactions for the New York Stock Exchange and the cash dividends we declared in each quarter.

	<u>High</u>	<u>Low</u> (Per share)	<u>Dividends</u>
2000			
First Quarter	\$42.3125	\$30.3125	\$0.2060
Second Quarter	52.5000	39.3750	0.2060
Third Quarter	67.5000	46.2500	0.2060
Fourth Quarter	74.2500	57.1300	0.2060
1999			
First Quarter	\$39.3750	\$30.6875	\$0.2000
Second Quarter	38.3750	31.9375	0.2000
Third Quarter	40.5000	34.4375	0.2000
Fourth Quarter	43.4375	33.3750	0.2000

In January 2001, our Board of Directors declared a quarterly dividend of \$0.2125 per share of common stock, payable on April 2, 2001, to stockholders of record on March 2, 2001. Future dividends will be dependent upon business conditions, earnings, our cash requirements, and other relevant factors.

In June 1999, our stockholders approved an increase in our authorized common stock to 750 million shares. We also rescinded our common stock repurchase program which authorized us to repurchase up to 10 million shares in order to meet a requirement to treat our 1999 merger with Sonat as a pooling of interests under generally accepted accounting principles.

We have an odd-lot stock sales program available to stockholders who own fewer than 100 shares of our common stock. The voluntary program offers these stockholders a convenient method to sell all of their odd-lot shares at one time without incurring any brokerage costs. We also have a dividend reinvestment and common stock purchase plan available to all of our common stockholders of record. The voluntary plan provides our stockholders a convenient and economical means of increasing their holdings in our common stock. Neither the odd-lot program nor the dividend reinvestment and common stock purchase plan have a termination date, however we may suspend either at any time. You should direct your inquiries to Fleet National Bank, our exchange agent.

ITEM 6. SELECTED FINANCIAL DATA

	Year Ended December 31,				
	2000	1999	1998	1997	1996
	(In millions, except per common share amounts)				
Operating Results Data: ⁽¹⁾					
Operating revenues ⁽²⁾⁽³⁾	\$21,950	\$10,709	\$9,560	\$10,184	\$6,597
Merger-related and asset impairment charges	91	557	15	50	99
Ceiling test charges ⁽⁴⁾	—	352	1,035	—	—
Income (loss) before extraordinary items and cumulative effect of accounting change	582	(242)	(306)	405	294
Basic earnings (loss) per common share before extraordinary items and cumulative effect of accounting change	2.53	(1.06)	(1.35)	1.81	1.61
Diluted earnings (loss) per common share before extraordinary items and cumulative effect of accounting change	2.44	(1.06)	(1.35)	1.77	1.59
Cash dividends declared per common share	0.82	0.80	0.76	0.73	0.70
Basic average common shares outstanding	230	228	226	224	183
Diluted average common shares outstanding	243	228	226	229	185

	As of December 31,				
	2000	1999	1998	1997	1996
	(In millions)				
Financial Position Data: ⁽¹⁾					
Total assets ⁽³⁾	\$27,445	\$16,667	\$14,455	\$14,784	\$13,206
Long-term debt, less current maturities	5,606	5,223	3,692	3,404	3,251
Company-obligated preferred securities of consolidated trusts	625	325	325	—	—
Minority interest	2,331	1,368	374	380	347
Stockholders' equity	3,569	2,947	3,437	3,921	3,514

⁽¹⁾ Our operating results and financial position reflect the acquisition in June 1996 of Cornerstone Natural Gas, in December 1996 of El Paso Tennessee Pipeline (formerly Tenneco Inc.), in August 1998 of DeepTech International, and in December 2000 of PG&E's Texas Midstream operations. These acquisitions were accounted for as purchases and therefore operating results are included in our results prospectively from the purchase date.

⁽²⁾ We restated historical operating revenues due to the implementation in 2000 of Emerging Issues Task Force Issue No. 99-19, *Reporting Revenue Gross as a Principal versus Net as an Agent*, which provides guidance on the gross versus net presentation of revenues and expenses. These reclassifications impacted operating revenues and expenses, but had no impact on net income (loss) or earnings per share.

⁽³⁾ The increase to our 2000 operating revenues and total assets reflects the significant growth in our Merchant Energy operations.

⁽⁴⁾ Ceiling test charges are reductions in earnings that result when capitalized costs of natural gas and oil properties exceed the upper limit, or ceiling, on the value of these properties.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

General

Over the past several years, our business activities and operations have changed dramatically as a result of significant acquisitions, transactions, and internal growth initiatives, designed to enhance our ability to compete effectively in the global energy industry. These changes have significantly expanded our operating scope, our ability to generate operating cash flows and our needs for cash for investment opportunities. Consequently, we have substantially expanded our credit facilities and created other financing structures and facilities to meet our needs during this period. The more significant changes are discussed below.

Merger with The Coastal Corporation

In January 2001, we merged with The Coastal Corporation. We accounted for the merger as a pooling of interests and converted each share of Coastal common stock and Class A common stock on a tax-free basis into 1.23 shares of our common stock. We also exchanged Coastal's outstanding convertible preferred stock for our common stock on the same basis as if the preferred stock had been converted into Coastal common stock immediately prior to the merger. We issued a total of 271 million shares, including 4 million shares issued to holders of Coastal stock options. The total value of the transaction was approximately \$24 billion, including \$7 billion of assumed debt and preferred equity.

Coastal is a diversified energy holding company. It is engaged, through its subsidiaries and joint ventures, in natural gas transmission, storage, gathering, processing and marketing; natural gas and oil exploration and production; petroleum refining, marketing and distribution; chemicals production; power production; and coal mining. Coastal owns interests in approximately 18,000 miles of natural gas pipelines extending across the midwestern and the Rocky Mountain areas of the U.S. has proved reserves of 3.6 Tcfe. Coastal also has international and domestic interests in natural gas and oil producing properties, power generation plants, and crude oil refining facilities.

Purchase of Texas Midstream Operations

In late December 2000, we completed our purchase of PG&E's Texas Midstream operations for \$887 million, including the assumption of \$527 million of debt. We accounted for this acquisition as a purchase. The assets acquired consist of 7,500 miles of natural gas transmission and natural gas liquids pipelines that transport approximately 2.8 Bcf/d, nine natural gas processing plants that process 1.5 Bcf/d, and rights to 7.2 Bcf of natural gas storage capacity. These assets serve a majority of the metropolitan areas and the largest industrial load centers in Texas, as well as numerous natural gas trading hubs. These assets also create a physical link between our EPNG and TGP systems. In March 2001, Field Services sold some of these acquired natural gas liquids transportation and fractionation assets to Energy Partners. The assets sold include more than 600 miles of natural gas liquids gathering and transportation pipelines and three fractionation plants located in south Texas.

In December 2000, to comply with a Federal Trade Commission order, we sold our interest in Oasis Pipeline Company. Proceeds from the sale were \$22 million and we recognized an extraordinary loss of \$19 million, net of income taxes of \$9 million.

Merger with Sonat Inc.

In October 1999, we completed our merger with Sonat. In the merger, we issued one share of our common stock for each share of Sonat common stock. Total shares issued were approximately 110 million shares. In connection with a Federal Trade Commission order related to this merger, we sold our East Tennessee Natural Gas Company and Sea Robin Pipeline Company as well as our one-third interest in Destin Pipeline Company. Proceeds from the sales were approximately \$616 million and we recognized an extraordinary gain of \$89 million, net of income taxes of \$60 million. We accounted for the merger as a pooling of interests.

Merger-Related Costs and Asset Impairment Charges

As we have integrated the activities and operations of our mergers and acquisitions, we have incurred, and will continue to incur, charges that will have a significant impact on our results of operations, financial position and cash flows. These costs, which are of a non-recurring nature, will include employee severance, retention, and transition charges; write-offs or write-downs of duplicate assets; charges to relocate assets and employees; contract termination charges; and charges to align accounting policies and practices.

During the three year period ended December 31, 2000, we incurred charges related to the mergers with Coastal, Sonat, and Zilkha Energy. In September 2000, we announced a plan to geographically consolidate our pipeline operations with Coastal's following the completion of our Coastal merger. Under the consolidation plan, El Paso Natural Gas Company's operations will be relocated from El Paso, Texas to Colorado Springs, Colorado, and ANR Pipeline Company, a subsidiary of Coastal, will be relocated from Detroit, Michigan, to Houston, Texas. Along with this consolidation, we will also conduct numerous relocations among our various operating sites. All relocations under these plans are expected to be completed by mid-year 2001.

Upon our merger with Coastal, we issued approximately 4 million shares of our common stock in exchange for Coastal employee, former employee, and outside director stock options. The total charge in connection with this exchange was approximately \$278 million and will be included in our combined operations during the first quarter of 2001.

As a result of our merger with Coastal, we will also be required to sell our Midwestern pipeline system. Proceeds from the sale are expected to be approximately \$90 million, and will result in a before tax gain of approximately \$50 million. We expect to complete this sale in the second quarter of 2001.

Additionally, in the first quarter of 2001 Energy Partners sold its interest in several offshore assets. These sales consisted of interests in seven natural gas pipeline systems, a dehydration facility and two offshore platforms. Proceeds from these sales were approximately \$135 million and resulted in a loss to the partnership of approximately \$23 million. As additional consideration for these sales, we committed to pay Energy Partners a series of payments totaling \$29 million. This amount, as well as our proportional share of the losses on the sale of the partnership's assets, will be recorded as a charge in our income statement in the first quarter of 2001.

We do not anticipate the impact of the sale of our Midwestern system or the transactions by or with Energy Partners to have a material effect on our ongoing financial position, operating results, or cash flows.

On January 30, 2001, we completed an employee restructuring, which resulted in the reduction of 3,285 full-time positions through a combination of early retirements and terminations. These reductions occurred across all locations and business segments. These actions resulted in severance and termination charges, retention payments for employees retained in the combined organization, and the acceleration of employee benefits under existing benefit plans. Total charges in connection with these actions are estimated to be approximately \$890 million with a majority being recorded in the first quarter of 2001.

The total cost of our merger-related activities, as well as additional charges we will incur as we complete our evaluations of the contracts, operating assets, and accounting policies of the combined organization could range between \$1.6 billion and \$2 billion. This estimate is based on the costs we expect to record in the first quarter of 2001 and our preliminary estimates of additional costs we will incur. We expect that most of these charges will be recorded in 2001.

Also during the three year period ended December 31, 2000, we incurred a variety of asset impairment charges ranging from those as a result of rate filings within our regulated pipelines to write-downs of operating plants and contracts that were determined to be impaired. We also recorded write-downs of capitalized costs of our natural gas and oil properties under the full cost method of accounting in both 1998 and 1999.

Our merger-related costs and asset impairment charges are reflected in the results of operations discussed below for each of our segments. The table below provides a summary of our merger-related costs and asset impairment charges by each of our business segments, and in total, for each of the three years ended December 31:

	<u>2000</u>	<u>1999</u> (In millions)	<u>1998</u>
Merger-related costs and asset impairment charges			
Pipelines	\$—	\$ 90	\$ —
Merchant Energy	—	67	—
Field Services	11	8	—
Production	—	31	15
Segment total	11	196	15
Corporate and other	80	361	—
Consolidated total	<u>\$91</u>	<u>\$557</u>	<u>\$ 15</u>
Ceiling test charges—Production	<u>\$—</u>	<u>\$352</u>	<u>\$1,035</u>

Segment Results of Operations

Our business activities are segregated into four segments: Pipelines, Merchant Energy, Field Services, and Production. These segments are strategic business units that offer a variety of different energy products and services. During the fourth quarter of 2000, we combined our International segment with our Merchant Energy segment to reflect the ongoing globalization of the Merchant Energy strategy and its operating activities. In addition, these results do not include the impact of our merger with Coastal, which will not be reflected in our results of operations until 2001. Results of PG&E's Texas Midstream operations were reflected in our results as of the purchase date. We manage each of our segments separately as each requires different technology and marketing strategies. Since earnings on equity investments can be a significant component of earnings in several of our segments, we evaluate segment performance based on earnings before interest expense and taxes, or EBIT, instead of operating income.

To the extent possible, results of operations have been reclassified to conform to the current business segment presentation, although such results are not necessarily indicative of the results which would have been achieved had the revised business segment structure been in effect during those periods. Operating revenues and expenses by segment include intersegment revenues and expenses which are eliminated in consolidation. Because changes in energy commodity prices have a similar impact on both our operating revenues and cost of products sold from period to period, we believe that gross margin (revenue less cost of sales) provides a more accurate and meaningful basis for analyzing operating results for the Merchant Energy and the Field Services segments. For a further discussion of the individual segments, see Item 8, Financial Statements and Supplementary Data, Note 15.

The following table presents EBIT by segment and in total, including the merger-related costs and asset impairment charges discussed above, for each of the three years ended December 31:

	<u>2000</u>	<u>1999</u> (In millions)	<u>1998</u>
Earnings Before Interest Expense and Income Taxes			
Pipelines	\$ 822	\$ 719	\$ 811
Merchant Energy	563	3	28
Field Services	102	85	76
Production	196	(257)	(936)
Segment EBIT	<u>1,683</u>	<u>550</u>	<u>(21)</u>
Corporate and other expenses, net	<u>(133)</u>	<u>(359)</u>	<u>(31)</u>
Consolidated EBIT	<u>\$1,550</u>	<u>\$ 191</u>	<u>\$ (52)</u>